HARTELA CONTRACTORS LTD

v.

HARTECON JV SDN BHD & ANOR

COURT OF APPEAL, KUALA LUMPUR
GOPAL SRI RAM JCA
ABDUL MALEK AHMAD JCA
HAIDAR MOHD NOOR JCA
[CIVIL APPEALS NOS: W-02-38-1996 & W-04-30-1997]
16 APRIL 1999

CONTRACT: *Collateral contract - Statement made during negotiation - Feasibility study - Joint venture entered into based on feasibility study - Whether feasibility study flawed - Whether there was subsequent turn out of events showing falsity of feasibility study - Whether there was liability based on collateral contract*

ARBITRATION: *Proceedings - Evidence - Issue not raised in pleadings but canvassed by both parties at hearing - Whether issue should be considered by arbitrator - Whether arbitrator exceeded jurisdiction in making award based on consideration of such issue*

CONTRACT: *Joint venture - Fiduciary duty - Nature and scope of duty - Best endeavours clause - Duty to warn the other party of risks involved - Duty to use best endeavours to ensure success of joint venture - Breach of duty and consequences*

CONTRACT: *Joint venture - Fiduciary duty - Sale and purchase agreement between joint venture parties - Secret profits - Whether allowed - Whether sale and purchase agreement part of joint venture agreement - Whether relationship was between vendor and purchaser simpliciter*

ARBITRATION: *Award - Setting aside - Whether possible - Whether award final in the absence of contrary intention in arbitration agreement - Exceptions at common law and in statute - Error of law - Misconduct - Whether court has jurisdiction to set aside award based on wrong inferences of fact or consideration of inadmissible evidence*

The appellant ('Hartela'), a Finnish manufacturer of building materials which was seeking a joint venture partner in Malaysia, had presented a feasibility study ('the Study') to the 2nd respondent ('Ferrostaal'). Based on this Study, which recommended *inter alia* a central-factory instead of a movable on-site unit for the production of pre-cast concrete panels, Ferrostaal SB entered into a joint venture agreement ('the JV') with Hartela on 5 March 1983. On 23

March 1983, a circular resolution ('the CR') which dispensed with the original pre-requisites of the JV was passed, and its effect was that a factory would be set up even before any construction contract was secured or financing arranged. Hartela was aware of the risks emanating from the CR but did not advise against it. Meanwhile, the parties formed a joint venture company ('Hartecon').

In August 1983, Hartela and Hartecon entered into a contract ('the Contract') under which a plant and machinery were supplied and installed at Hartecon's factory and from which Hartela made a profit of RM924,000 ('the Profit'). Hartecon paid part of the purchase price and the balance was secured by a bank guarantee obtained by Ferrostaal. Hartela was entitled to make a call on the guarantee but only after the issuance of a certificate by a representative of Hartela ('Karenmaa') who was an employee of Hartecon. In September 1983, another agreement was drawn up whereby Hartecon was obliged to accept and follow the advice of Karenmaa.

As it transpired, Hartecon failed to obtain any construction contracts but the plant and machinery still had to be paid for. In August 1984, Karenmaa issued a certificate of completion thus triggering the payment clause in the Contract. Hartecon did not make payment and Hartela made a call on the guarantee which resulted in other creditors descending on Hartecon. In June 1985, Hartela terminated the JV. The parties then referred the ensuing disputes to arbitration which resulted in an award in favour of Ferrostaal and Hartecon. A second award was subsequently made in respect of the quantum to be paid by Hartela. Hartela's application to set aside the awards was refused by the High Court and it appealed on the following grounds: (i) there was no actual turn out of subsequent events that demonstrated the falsity of the opinion entertained by Hartela as to the feasibility of the JV. Thus, the arbitrator had misconducted himself by finding Hartela's forecast to be flawed by preferring the opinion of Ferrostaal's expert witness to that expressed by Hartela in the Study; (ii) the arbitrator had exceeded his jurisdiction in considering whether Hartela had a duty to advise against the CR as this issue was never pleaded in the statement of claim; (iii) the arbitrator had committed an error of law on the face of the award when he held that Hartela was under a duty to warn Ferrostaal of the dangers emanating from the CR; and (iv) the arbitrator's order to Hartela to disgorge the Profit was bad in law because the Contract was for the sale of goods, and a vendor is entitled to make profits.

Held:
Per Gopal Sri Ram JCA

[1a] The arbitrator found that Ferrostaal had entered into the JV on the strength of the Study. His approach to the question of law that arose before him was correct. The device of a collateral contract is one of the methods employed by the law to impose liability for a statement made in the course of negotiations preceding the making of a contract. The arbitrator's award did not reveal any errors of law or misconduct.

[1b] This was not a case where there had not been a turn out of events. As the arbitrator had found, upon the evidence, the Study failed to take into account matters of primary importance as a result of which there was an unfavourable turn out of events for Ferrostaal.

[2] The rule requiring arbitrators to decide only the issues raised by the pleadings is consonant with natural justice and the general principles of equity and good conscience. However, although the issue whether Hartela had a duty to advise against the CR was never pleaded in the statement of claim, it was much canvassed by both parties during the arbitration. Therefore, the arbitrator had to consider the issue and did not exceed his jurisdiction when he did so.

[3] The parties to a joint venture stand in a fiduciary position towards each other; where there is reliance by one party on the skill or expertise professed by the other in the subject matter of the enterprise, there is a duty upon that other to use his best endeavours to ensure the success of the venture. Equity will imply such an obligation in the absence of an express term to that effect. Here, the JV even had a 'best endeavours clause'. And as the CR was not in the best interests of Hartecon, Hartela should have warned Ferrostaal of the risks. The arbitrator was thus right in holding that Hartela had breached its fiduciary duty in failing to do so.

[4] The relationship between Hartela and Ferrostaal was not one of vendor and purchaser simpliciter. The Contract was part and parcel of the JV. Hartela as a joint venturer and a fiduciary was not entitled to make secret profits at the expense of Ferrostaal.

[5] The arbitrator took a broad approach in making the second award in respect of quantum. Hartela's complaints herein did not fall within the scope of the court's jurisdiction to interfere.

[6] In the absence of a contrary intention in the agreement to arbitrate, the award of the arbitrator is final, binding and conclusive, and cannot be challenged on the ground that it is erroneous. One exception at common law is where there is an error of law on the face of the award. Under s. 24(2) of the Arbitration Act 1952, the court may set aside the award if the arbitrator has misconducted himself or the proceedings. The court, however, is **not** seised of jurisdiction to set aside the award on the ground that wrong inferences of fact have been drawn or that inadmissible evidence has been let in and acted upon.

[Appeals dismissed.]

Case(s) referred to:

Aberdeen Ry Co v. Blaikie Brothers [1854] 1 Macq 461 ***(refd)***

Boustead Trading (1985) Sdn Bhd v. Arab-Malaysian Merchant Bank Bhd [1995] 4 CLJ 283 ***(foll)***

Champsey Bhara Co v. The Jivraj Balloo Spinning & Weaving Co Ltd AIR [1923] PC 66 ***(foll)***

Dick Bentley Productions Ltd v. Harold Smith (Motors) Ltd [1965] 1 All ER 65 ***(foll)***

Esso Petroleum Co Ltd v. Mardon [1976] QB 801 ***(foll)***

Ganda Edible Oils Sdn Bhd v. Transgrain BV [1987] 2 CLJ 394 ***(dist)***

Hodgkinson v. Fernie [1857] 3 CBNS 189 ***(foll)***

Jeuro Development Sdn Bhd v. Teo Teck Huat (M) Sdn Bhd [1998] 3 CLJ Supp 366 ***(foll)***

Keech v. Sandford [1726] Sel Cas Ch 61 ***(refd)***

Malayan Insurance Incorporated v. Chek Brothers Construction Company [1973] 1 MLJ 185 ***(refd)***

Meinhard v. Salmon [1928] 249 NY 456 ***(refd)***

Newacres Sdn Bhd v. Sri Alam Sdn Bhd [1991] 3 CLJ 2781 ***(refd)***

Puri Construction Pvt Ltd v. Union of India AIR [1989] SC 777 ***(foll)***

Regal (Hastings) Ltd v. Gulliver [1942] 1 All ER 378 ***(foll)***

Shah Alam Properties v. Abdul Razak Abu Samah (Civil Appeal No: 03-43-98) ***(refd)***

Sykt Pemborong Pertanian & Perumahan v. Federal Land Development Authority [1971] 2 MLJ 210 ***(refd)***

Tan Swee Hoe Co Ltd v. Ali Hussein Bros [1980] 2 MLJ 16 ***(foll)***

Union of India v. Rallia Ram AIR [1963] SC 1685 ***(foll)***

Legislation referred to:

Arbitration Act 1952, s. 24(2)

For the appellant - Lim Chor Pee (Lathika Prabakaran with him); M/s Chor Pee Anwarul & Co

For the respondents - N Rajendra (Zaheeda Ariff with him); M/s Azman Davidson & Co

Reported by Cindy Chan

a

JUDGMENT

Gopal Sri Ram JCA:

Introduction

b There are two appeals before us. They concern two arbitration awards relating to a dispute. In the first of these, the arbitrator found liability in favour of the respondents. In the second, he assessed quantum. The first appeal is against refusal by the High Court to set aside the award on liability. The second appeal is directed against the order of the High Court refusing to set aside the award on quantum. The facts relevant to these appeals may be shortly stated.

c

Facts And Background

The appellant ("Hartela") is a Finnish company. It has considerable experience in the manufacture of pre-cast concrete panels used in the construction of pre-
d fabricated houses. Hartela wanted to do business in Malaysia. It identified the second respondent ("Ferrostaal") as a joint venture partner. Hartela then carried out a feasibility study which was reduced into writing. It is a document with a very long title. I will refer to it as "the Techno-Economic Study". The Techno-Economic Study contained various statements about the viability of
e producing pre-cast concrete panels in Malaysia. It painted a very rosy picture about the profits that could be made. Ferrostaal was impressed by what the Techno-Economic Study said. Indeed, as the arbitrator found, Ferrostaal was induced by and acted upon the Techno-Economic Study on the strength of which it entered into a joint venture agreement with Hartela on 5 March 1983. But, as the arbitrator found, the Techno-Economic Study was fatally flawed.
f It suggested a central factory concept instead of a readily movable production unit. That, of course, would materially affect transport costs. But the Techno-Economic Study did not take this into account.

A few days later, on 23 March 1983, a circular resolution was passed which
g materially altered the original basis of the joint venture. The joint venture agreement provided for the obtaining of a contract to construct houses, finance for the project and a suitable factory site before the injection of further capital. The circular resolution changed all this by completely dispensing with these essential pre-requisites. The effect was that the factory would be set up even
h before a single construction contract had been secured and financing arranged. The arbitrator found that Hartela knew and recognised the danger in the venture failing as a result of this change. Hartela had all the expertise. It was aware of the risks which the change entailed. But it did not advice against the change made by the resolution. As it happened, the change which the circular resolution made was to have disastrous effects.

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In the meantime, the parties formed a joint venture company. It is the first respondent ("Hartecon"). There were three shareholders in Hartecon; Ferrostaal which held 70%, Hartela which held 15% and Finnish Fund for Industrial Development Corporation Ltd. ("Finnfund") which held the remaining 15%.

In August 1983 Hartela and Hartecon entered into another agreement. The arbitrator referred to it as "the Purchase Contract". That is because it described Hartela as the seller and Hartecon as the buyer. Under the Purchase Contract Hartela was to supply and install plant and machinery at a site provided by Hartecon. Although Hartela was a joint venture partner of Ferrostaal and a shareholder of Hartecon, it did not expose itself to any liability for the payment of the plant and machinery. Hartecon made part payment of the purchase price. The balance was secured by a bank guarantee obtained by Ferrostaal from Perwira Habib Bank Bhd. If there was a call on the guarantee by Hartela, it would be Ferrostaal alone that would be liable. But Hartela was only entitled to make a call upon the guarantee after the issue of a certificate by Hartela's representative in Hartecon. That representative was a gentleman by the name of Mr. Karenmaa. He was an employee of Hartecon. But he was Hartela's man.

In September 1993, yet another agreement was drawn up. It is called "the Technical Know-How Agreement". By its terms, Hartecon was obliged to accept and follow the advice given by Mr. Karenmaa.

As matters turned out the joint venture was a failure. Hartecon did not obtain any contracts for the construction of houses. But its factory had been set up. Hartela had brought in the machinery and this had to be paid for. On 25 August 1984, Mr. Karenmaa issued a certificate to the effect that the machinery was substantially complete. Hartecon had no knowledge of the existence of this certificate. The issuance of the certificate triggered the payment clause in the purchase contract. Hartecon did not pay Hartela then presented its bill to Perwira Habib Bank and called on the guarantee. That caused the other creditors to descend *en masse* on Hartecon. Then, by a telex dated 19 June 1985, Hartela terminated the joint venture agreement.

Disputes later arose and the parties referred these for arbitration to Dato' Dr. Peter Mooney, a lawyer with much knowledge of and experience in commercial law. After a fairly lengthy hearing at which witnesses were called by both sides, the arbitrator made an award in which he found for Hartecon and Ferrostaal on several of the claims made by them. It is a reasoned award which comprehensively sets out and deals with all the issues in controversy. Much later, the arbitrator made a second award in which he assessed quantum. Hartela then moved the High Court to have both awards set aside. The judge who heard the applications dismissed them. It is against those orders that the present appeals have been brought.

So much for the history of the matter.

Heads Of Argument

Mr. Lim Chor Pee of counsel for Hartela has in his usual careful manner advanced a number of arguments in support of both appeals. They may be readily summarised under four heads.

1. The breach of the collateral warranty;
2. Breach of fiduciary duty;
3. Excess of jurisdiction;
4. The award for secret profit

Before I deal with each of these heads of argument, I think it useful to remind myself of the parameters within which a court must act in an application to set aside the award of an arbitrator.

The Role Of The Court

The general rule at common law is that, absent a contrary intention in the agreement to arbitrate entered into between the parties to a controversy, the award of an arbitrator is final, binding and conclusive. It may not be challenged merely on the ground that it is erroneous. As Shah J, said in *Union of India v. Rallia Ram* AIR [1963] SC 1685, at p. 1691:

> An award being a decision of an arbitrator whether a lawyer or a layman chosen by the parties, and entrusted with power to decide a dispute submitted to him is ordinarily not liable to be challenge on the ground that it is erroneous ... The Court may also set aside an award on the ground of corruption or misconduct of the arbitrator, or that a party has been guilty of fraudulent concealment or wilful deception ... The award of the arbitrator is ordinarily final and conclusive, unless, a contrary intention is disclosed by the agreement. The award is the decision of a domestic tribunal chosen by the parties, and the Civil Courts which are entrusted with the power to facilitate arbitration and to effectuate the awards, cannot exercise appellate powers over the decision. Wrong or right the decision is binding if it be reached fairly after giving adequate opportunity to the parties to place their grievances in the manner provided by the arbitration agreement.

So jealously did the common law guard against curial interference with private arbitrations that it was most reluctant to create exceptions to the general rule. The policy of the common law is reflected in the judgment of Williams J, in *Hodgkinson v. Fernie* [1857] 3 CBNS 189 where he said:

> The law has for many years been settled, and remains so at this day that, where a cause or matters in difference referred to an arbitrator a lawyer or a layman, he is constituted the sole and final judge of all questions both of law and of fact. ... The only exceptions to that rule are cases where the award is the result of corruption or fraud, and one other, which though it is to be regretted is now, I think firmly established *viz.*, where the question of law necessarily arises on the face of the award or upon some paper accompanying and forming part of the award. Though the propriety of this latter may very well be doubted I think it may be considered as established.

Thus, the common law as a very limited exception grudgingly allowed a court to intervene and set aside an award on the face of which there appeared an error of law. That is an important exception that prevails until today. In *Champsey Bhara Co. v. The Jivraj Balloo Spinning & Weaving Co. Ltd.* AIR [1923] PC 66, Lord Dunedin, when delivering the advice of the Board, explained the breadth of this limited common law jurisdiction over arbitration awards. He said (at p. 69):

> An error in law on the face of the award means, in their Lordships' view, that you can find in the award or a document actually incorporated thereto, as for instance, a note appended by the arbitrator stating the reasons for his judgment, some legal proposition which is the basis of the award and which you can then say is erroneous. It does not mean that if in a narrative a reference is made to a contention of one party that opens the door to seeing first what that contention is, and then going to the contract on which the parties' rights depend to see if that contention is sound.

Quite apart from the common law, the jurisdiction of the ordinary courts in the environment of private arbitration stems also from statute. Thus, s. 24(2) of the Arbitration Act 1952 confers jurisdiction upon the High Court to set aside an award for misconduct by an arbitrator. "Misconduct" in this context

> is used in its technical sense as denoting irregularity and not moral turpitude. It includes failure to perform the essential duties which are cast on an arbitrator as such, for instance, failure to observe the rules of natural justice, appearance of bias or partiality. It also includes any irregularity of action which is not consonant with the general principles of equity and good conscience. These illustrations are not meant to be exhaustive. But failure to analyse and appraise the evidence does not vitiate the award on the ground of misconduct. It is only when the evidence is material, relevant and had gone to affect the award that the award will be vitiated. In my judgment the plaintiffs' complaint is sustainable only if the failure to do so had occasioned some irregularity causing a miscarriage of justice that is apparent on the face of the award. (per Raja Azlan Shah J., (as he then was) in *Sharikat Pemborong Pertanian & Perumahan v. Federal Land Development Authority* [1971] 2 MLJ 210, at p. 211.)

I have searched in vain for a better description of what Parliament meant by the use of the expression "misconduct" in the Act of 1952.

In my judgment the jurisdiction to set aside or to remit an arbitrator's award whether at common law or under statute is one that should be exercised with great care and with a proper sense of responsibility. One may do well to keep in mind the words of Sharma J, in *Puri Construction Pvt. Ltd. v. Union of India* AIR [1989] SC 777, at p. 780:

> When a court is called upon to decide the objections raised by a party against an arbitration award, the jurisdiction of the court is limited, as expressly indicated in the Arbitration Act and it has no jurisdiction to sit in appeal and examine the correctness of the award on merits.

At this juncture there is one other case which I think I ought to mention. It was not cited by either side. But I came across it while consulting the authorities upon the subject. It is a case that, on a first reading, caused me some difficulty. It is *Ganda Edible Oils Sdn Bhd v. Transgrain BV* [1988] 1 MLJ 428. Being a decision of the Supreme Court, it has binding effect. There, Syed Agil Barakbah SCJ said (at p. 431):

> The questions that should have arisen before the judge were (1) whether the arbitrator made wrong inferences of fact from the evidence including the four telexes which were incorporated in the award and (2) whether the arbitrator had erroneously construed the two sections.
>
> In the first place, we are satisfied that the arbitrator had considered all the relevant evidence and had not made wrong inferences of fact. As regards the second point, we are also satisfied after careful consideration that the arbitrator has construed the two sections correctly in the light of the facts and surrounding circumstances of the case. We also bear in mind that even if we could come to a different conclusion on the matter, we fail to see in the award that the arbitrator has proceeded illegally either by deciding on inadmissible evidence or applying the wrong principles of construction which the law does not recognise.

Putting aside for a moment the reference in the foregoing passage to the erroneous construction of the statute in question, which may well be regarded either as an error of law on the face of the award or as misconduct, the Supreme Court speaking through Syed Agil Barakbah SCJ appears at first blush to recognise an ability in a court to intervene on the ground that an arbitrator had made wrong inferences of fact or had considered inadmissible evidence. On the authorities that I have had the advantage of consulting, such a wide jurisdiction does not appear to exist. However, on a more careful reading of the case it is clear that the learned judge was merely adverting to the arguments made before the Supreme Court in that case and repelling a suggestion by counsel that the arbitrator there had drawn erroneous factual

inferences or had considered inadmissible evidence. In my view, the *Ganda Edible Oils* case is not, and should not be read, as authority for the proposition that the ordinary courts are seised of jurisdiction to remit or set aside the award of an arbitrator on the ground that wrong inferences of fact had been drawn or that inadmissible evidence had been let in and acted upon. To do so would amount, in my respectful view, to the unwarranted exercise of an appellate function over private arbitrations which, of course, courts do not have. So far as inferences of fact are concerned, these really fall within the realm of the merits of the particular dispute and are of no concern of a court when considering an application to set aside an award. See, *Puri Construction Pvt. Ltd. v. Union of India (ibid).* And so far as questions of evidential admissibility are concerned, it has been always recognised that the technical rules of evidence that govern a trial in the ordinary courts do not apply to arbitrations. In this regard, I would refer to and readily accept as correct the following statement of the law by Augustine Paul J, in *Jeuro Development Sdn Bhd v. Teo Teck Huat (M) Sdn Bhd* [1998] 6 MLJ 545, at p. 552:

> Proceedings before arbitrators are governed by s. 13 of the Act which provides for, *inter alia*, examination upon oath or affirmation. When witnesses are required to be examined on oath *viva voce* examination is intended and the taking of evidence by affidavit is not a sufficient compliance with the provisions (see *Banks v. Banks* [1835] 1 Gale 46). It is true that rules of evidence do not apply to proceedings before arbitrators. This is provided by s. 2 of the Evidence Act 1950 which reads as follows:
>
> > This Act shall apply to all judicial proceedings in or before any Court, but not to affidavits presented to any Court or officer nor to proceedings before an arbitrator.
>
> The Evidence Act 1950 is therefore not intended to apply to proceedings before an arbitrator (see *Municipal Corp of Delhi v. Jagan Nath Ashok Kumar* [1987] 4 SCC 497; *Hazi Ebrahim Kassam Cochinwalla v. Northern India Oil Industries* AIR [1951] Cal 230). Thus, an arbitrator is not bound by the strict rules of evidence, and it is not a valid objection to the proceedings if he has departed from some technical rule of the Evidence Act 1950 (see *Suppu v. Govindacharyar* [1887] 11 Mad 85; *Howard v. Wilson* 4 Cal 231). ... A departure from the rules of the Evidence Act 1950 does not per se amount to misconduct, unless the rule of evidence violated is one which is based on natural justice and an infringement of it is, therefore, repugnant to one's sense of justice and fairness.

With that I now turn to address my mind to the three main heads of argument advanced by Mr. Lim Chor Pee.

Collateral Warranty

As I earlier said, the arbitrator in the present instance found that Ferrostaal had entered into the joint venture agreement upon the strength of the Techno-Economic Study. This is how he put it:

> The study in my view was seriously flawed. It misled Ferrostaal. It convinced Ferrostaal of the viability of the factory project and on the basis of it they decided to enter into a Joint venture with Hartela.

Having made this finding he applied the statement of principle contained in the judgment of Lord Denning M.R. in *Esso Petroleum Co. Ltd. v. Mardon* [1976] QB 801. The Master of the Rolls there said (at p. 817):

> Ever since *Heilbut, Symons & Co v. Buckleton* [1913] AC 30, we have had to contend with the law as laid down by the House of Lords that an innocent misrepresentation gives no right to damages. In order to escape from that rule, the pleader used to allege ... that the misrepresentation was fraudulent, or alternatively a collateral warranty. At the trial we nearly always succeeded on collateral warranty ... [There] have been many cases ... where we have readily held a representation – which induces a person to enter into a contract – to be a warranty sounding in damages. I summarized them in *Dick Bentley Productions Ltd v. Harold Smith (Motors) Ltd* [1965] 1 All ER 65 ... In the present case it seems to me that there was a warranty that the forecast was sound, that is, Esso made it with reasonable care and skill. That warranty was broken ... For this they are liable in damages ...

In the earlier case of *Dick Bentley Productions Ltd v. Harold Smith (Motors) Ltd* [1965] 1 All ER 65, Lord Denning M.R. said (at p. 67):

> Looking at the cases once more, as we have done so often, it seems to me that if a representation is made in the course of dealings for a contract for the very purpose of inducing the other party to act on it, and it actually induces him to act on it by entering into the contract, that is *prima facie* ground for inferring that the representation was intended as a warranty. It is not necessary to speak of it as being collateral. Suffice it that the representation was intended to be acted on and was in fact acted on.

That the position at our common law is no different is made clear by the decision of the former Federal Court in the leading case of *Tan Swee Hoe Co. Ltd. v. Ali Hussein Bros.* [1980] 2 MLJ 16, where at p. 18 Raja Azlan CJ (as he then was) said:

> Although it is trite law that parol evidence is not admissible to add to, vary or contradict a written agreement, a technical way of overcoming the rule is by invoking the doctrine of collateral contract or collateral warranty. *Chitty on Contracts* (24th ed) (para 674) put it this way:

> An assurance given in the course of negotiation may therefore give rise to a contractual obligation, provided that an intention to be bound can be shown. The rules of evidence, however, frequently prevent such an assurance from being incorporated as part of a subsequent written agreement, since extrinsic evidence is as a general rule not admissible to vary or add to the terms of a written contract. As a result, the courts have been prepared in some circumstances to treat the assurance as a separate contract, collateral to the main transaction. In particular, they will do so where one party refuses to enter into the contract unless the other gives him an assurance on a certain point.
>
> In our view there is a growing body of authority which supports the proposition that a collateral agreement can exist side by side with the main agreement which it contradicts.

In my judgment, the arbitrator's approach to the question of law that arose incidentally before him was correct. It is trite that the device of a collateral contract is one of the methods employed by the law to impose liability for a statement made in the course of negotiations preceding the making of a contract. Very recently, in *Shah Alam Properties v. Abdul Razak Abu Samah* (Civil Appeal No. 03-43-98, unreported) this court has set out the propositions of law that operate in the environment of pre-contractual statements. I find it unnecessary to repeat what was there said. Suffice to say that the arbitrator's award with which we are here concerned does not reveal an error of law nor misconduct in the context of the present discussion.

Mr. Lim Chor Pee says that all this is very well, but that in all the other cases of collateral contract there was a turn out of events which were factually different from that appearing in the pre-contractual statement. For example, in the case of Mr. Mardon, Esso's representation that the throughput or estimated annual consumption would be 200,000 gallons per annum from the third year of operation turned out to be false because of the way in which the local authority required the petrol pumps to be located at the site. Esso ought to have revised its estimate when it had knowledge of the true position. It did not. Instead it maintained its original figures. That led to failure of the enterprise.

But, says Mr. Lim, that is not what happened in the present case. According to him, there was no actual turn out of subsequent events that demonstrated the falsity of the opinion entertained by Hartela as to feasibility of the joint venture. What Ferrostaal did was to try and establish a flaw in the Techno-Economic Study through the opinion evidence of another expert. Counsel argues that the arbitrator misconducted himself by finding Hartela's forecast to be flawed by preferring the opinion of Ferrostaal's expert witness to that expressed by Hartela in the Techno-Economic Study.

When I first heard Mr. Lim's argument, I thought that there was much force in it. However, after hearing Mr. Rajendra's response, and having read and re-read the award, I am more than satisfied that Mr. Lim's submission is without merit. For, this is not a case where there was not a turn out of events. As the arbitrator found, acting upon abundant evidence, the Techno-Economic Study did not take into account certain matters of primary importance as a result of which there was an unfavourable turn out of events for Ferrostaal. His conclusions may be summarised as follows.

Hartela had all the relevant knowledge base for the construction of prefabricated houses. It was the expert in that field. It knew that there were two methods of producing the elements for prefabrication. One was very expensive; the other less expensive. The expensive method was to have a factory with special machinery to prefabricate the elements and have these conveyed to a housing site. The cheaper method was to cast the elements at the site. Hartela had substantial projects in Egypt for the construction of prefabricated homes. For these it used the cheaper method and cast the elements at the construction site. Despite its expertise Hartela did not suggest the on site method of production in the Techno-Economic Study. It only recommended the central factory concept. Hartela's own witness, one Mr. Nevaste, said in his evidence that the central factory concept was put forward in the Techno-Economic Study "without any thorough analysis". The arbitrator described Mr. Nevaste's statement as "extraordinary". I agree.

The central factory concept recommended by Hartela and accepted by Ferrostaal had a snowballing effect on transport costs. The arbitrator dealt with it in this way:

> The second serious flaw in the study is this. Prefabricated houses are favoured for low-cost and medium-cost housing because of their speed and economy of construction. All that has to be done after the site is prepared is to put the panels together, which is not a lengthy process. This necessarily entails that the panels, if not manufactured on the site – the process that entirely failed to be considered in the study – must be on continuous delivery to the site so as not to keep the construction team waiting. This means that the necessary transport must be available to the construction company it is remarkable that there is no discussion of this crucial requirement in the study. The study states that the market area would be 150 km radius 150 km is a considerable distance. How long does it take a specially designed vehicle carrying prefabricated panels weighing several tons to travel 150 km and how long does it take to return, collect another load and get back to the site? One lorry obviously is quite insufficient if there are not to be constant and lengthy delays in construction. How many lorries would be necessary? It does not appear that any thought was given to this. If thought was given there is no evidence of it in the study. $500,000 is allowed for vehicles. The study contains no indication of how this

figure was arrived at. Does it contain provision for transport for the managing Director, for an Engineer or site supervisors? How much would a special lorry cost and how many, allowing for other transport, can one purchase for $500,000. In the absence of any details or discussion in the study one can only assume that the figure of $500 000 is a random figure and that there has been no serious consideration of the logistics involved. Indeed despite the 150 km radius, mentioned in an early part of the report as the radius of the factory, when consideration is given to site costs at the later part of the report the cost is estimated on the basis that the transport distance is 1.5 km, one hundredth of what the report earlier said was the radius. Mr Nevaste explained this by saying that their partners said they could get a large project and put the factory beside it. This is not convincing. No details were given of this "large project" and the study does not bear to be based on a particular project. It does say the factory plot is presumed to be in connection with the construction site but any construction site is limited and if there is to be a factory as opposed to on-site construction the factory must serve a wider area and not merely one construction site. And that is what the study is talking about when it speaks of 150 km radius. A study which says the main market area should be within a radius of 150 km, gives no indication of what capital costs would be incurred in servicing this area and confines its estimate of onsite costs to a radius one-hundredth that of the stated radius is seriously defective.

There one has it. The central factory concept recommended by Hartela proved to be disastrous for Ferrostaal and Hartecon. And that is the turn out of events which Mr. Lim says is lacking in the present case. The arbitrator was unable to see any difference in principle between Mr. Mardon who found himself in financial straits as a result of relying upon Esso's erroneous forecast and Ferrostaal which lost all its investment in Hartecon by reason of Hartela's negligent recommendation of the central factory concept. I find myself in the same position. In my view, therefore, the award suffers from no error of law, nor has there been any misconduct by the arbitrator, on this count.

That brings me to the second head of argument. Because of the way in which the submissions were addressed to us, it is closely connected with the third head of argument. I will therefore take them together, but not in the same order.

Fiduciary Duty And Excess Of Jurisdiction

The complaint under these two heads has to do with the circular resolution of 23 March 1983. As I earlier said, this resolution fundamentally changed the basis of the joint venture. To recall, the joint venture agreement envisaged the obtaining of a contract to construct and the arrangement of finance before the establishing of a central factory. The circular resolution in question did away with the first two stages. It took Hartecon straight into the third stage of the joint venture, namely, the establishment of a factory. The arbitrator took the view that Hartela, knowing of the risk created by the change ought to have advised Ferrostaal about it. This is what he said:

> Should Hartela have warned Ferrostaal of the danger involved in the change? Encik Halim [of Ferrostaal] seemed to be confident of getting a construction contract but a prudent businessman considers all the possibilities. Supposing Hartecon didn't immediately get a construction contract? We all know now that this spelled ruin for the venture. Encik Halim was a businessman but he knew nothing of prefabricated concrete casting. The study, on the basis of which he was taking his decisions, was seriously flawed and its economics gave a distorted picture of the true position. Had he been properly advised, would he have made the proposal? I cannot think so. Encik Halim impressed me as a very able and intelligent person. This is obvious from his history and from an examination of his extremely well-written and comprehensive letters and telexes. Mr. Norri [Hartela's lawyer] also found him 'a very impressive person'. Mr. Newton [Ferrostaal's expert witness] said it was unbelievable that anyone could build a factory without a large project. 'I could not in my wildest dreams' he said 'believe it could possibly work in Malaysia'. Mr. Norri, no Malaysian expert nor PCC expert, was 'very astonished' and knew the change involved great risk. Surely, this being the case, Hartela, the PCC authority on whose expertise Ferrostaal was relying, ought to have pointed out the grave implications which the change involved, implications which were by no means clear from their Techno-Economic Study. Hartela claimed to have 'all the necessary know-how' and undertook in the Joint Venture Agreement 'to exercise its best endeavours at all times to promote the interest of the company'. It is not to be doubted that it possessed the know-how but was it when a far-reaching change in the basis of the venture was proposed, a change which, in fact, led to the ruin of the company, exercising its best endeavours by going along with this and saying nothing to Ferrostaal of the grave risks which even their own lawyer was worried about and drew to their attention? I do not think so. In my view Hartela had a duty to point out to Ferrostaal the strong objections to the change and to advise them firmly against it. Had they done so, the circular resolution would very likely not have been passed and the subsequent unfortunate history would probably never have taken place.

Mr. Lim has submitted that this portion of the award cannot stand for two reasons. First, because the arbitrator exceeded his jurisdiction. Counsel has said that the issue of whether there was a duty to advise against the circular resolution was never pleaded in the statement of claim delivered by Hartecon and Ferrostaal. It was therefore never submitted to the arbitrator for an award. Accordingly, the arbitrator, says Mr. Lim, exceeded his authority in making an award upon this issue.

Counsel submitted that an arbitrator is bound to decide only upon the issues submitted to him by the disputants. An award made upon an issue not so submitted is bad for excess of authority on the part of the arbitrator. In support of these submissions Mr. Lim relied on the decision of the Singapore Court of Appeal in *Malayan Insurance Incorporated v. Chek Brothers Construction Company* [1973] 1 MLJ 185 where Chua J said at (p. 186):

From the pleadings it is quite clear that when the parties went before the arbitrator they had agreed that the arbitrator should, apart from the question of quantum, decide the issue of liability on the two defences pleaded, namely (1) that the exclusion clause (f) in the policy excludes liability for damage caused by pile driving, subsidence or demolition or resulting from the removal or weakening of support and (2) that the respondent had failed to take reasonable and proper precautions to prevent the accident as required by the outside liability provisions.

The authorities show that an arbitrator must decide the question or questions submitted to him for decision and that he must not go beyond that.

In *Bond Air Services v. Hill* [1955] 2 All ER 476 Lord Goddard CJ in the course of his judgment said (at p. 479):

> I do not think it can be doubted that, ordinarily, it is for the underwriter to prove a breach of condition, at least where he is not contending that the policy is void on the ground that there has been a breach of condition precedent to the formation of the policy. So, too, it is for him to prove an exception. The difference between a condition and an exception is that the former places some duty or responsibility on the assured, while the latter restricts the scope of the policy. That it is for the insurers who allege that the conditions were broken to prove it, has, I think, always been accepted, at least since Parke, B's judgment in *Barrett v. Jermy* ([1849] 3 Exch 535 at p. 452).

In *Re Green & Co and Balfour, Williamson & Co* [1890] 63 LT 325 there was a contract for the sale of tinned salmon which provided 'quality guaranteed good, merchantable and equal to average of the spring pack of 1889 season CR Salmon ... Any dispute to be settled by arbitration'. Differences having arisen, arbitration proceedings took place. The arbitrators found that the salmon was not of the quality guaranteed, and directed, in accordance with an alleged custom in the Liverpool market, that the buyers should take delivery, subject to an allowance being made. It was held, by the Court of Appeal, that the only question referred was whether or not the goods were of the guaranteed quality; that the arbitrators had therefore exceeded their jurisdiction and that the award should be remitted to them for their reconsideration.

It was, therefore, for the appellant to plead it specifically in his points of defence if he had wished to submit to the arbitrator the construction of clause (b) of the outside liability provisions of the policy. This he failed to do and therefore the arbitrator had no jurisdiction to deal with that clause.

In our judgment the learned Chief Justice was correct in holding in this case that the arbitrator had gone beyond his jurisdiction in dismissing the respondent's claim on a ground which was not specifically pleaded and which was not referred to him.

Mr. Lim then drew our attention to the following passage in the award which he says brings home the point he is making, namely, that the arbitrator exceeded his jurisdiction by deciding upon an issue not submitted to him in the pleaded case:

> There is a submission on behalf of Ferrostaal on the change in the basis of the joint venture effected by the circular resolution of 23 March 1983 which revoked stage 2 of the Project Description. This issue is not spelled out very clearly in the third amended statement of claim. **However it was much canvassed by both parties in the adduction of evidence during the hearing** and I think 1 must deal with it. (Emphasis added.)

I am prepared for the moment to accept the view expressed by the Court of Appeal of Singapore in *Malayan Insurance Company Inc. v. Chek Brothers Construction Company (ibid)*. I do so because there is absent an argument by Mr. Rajendra that the view expressed by Chua J, takes the law relating to pleadings before an arbitrator too far. Yet, I am satisfied that there has been no excess of jurisdiction or other misconduct by the arbitrator in the present instance.

In my view, the rule that requires arbitrators to decide only the issues raised by the pleadings is consonant with the requirements of natural justice and with the general principles of equity and good conscience. (See *Sharikat Pemborong Pertanian & Perumahan v. Federal Land Development Authority (ibid)*). And I consider it to be a principle of universal application to all forms of dispute resolution, that an arbiter, whether private or public, is entitled, if not obliged, to consider and deal with a point that is pursued evidentially and in argument by parties to a controversy. The decision of the Federal Court in *Boustead Trading (1985) Sdn. Bhd. v. Arab-Malaysian Merchant Bank Bhd.* [1995] 3 MLJ 331 exemplifies the application of this general principle to pleadings in ordinary litigation. It was there said (at p. 342), in relation to a plea of estoppel, that

> ... where there is no pleaded case of estoppel, but there is let in, without any objection, a body of evidence to support the plea, and argument is directed upon the point, it is the bounden duty of a court to consider the evidence and the submissions and come to a decision on the issue. It is no answer, in such circumstances, to say that the point was not pleaded: *Oversea-Chinese Banking Corp Ltd v. Philip Wee Kee Puan* [1984] 2 MLJ 1.

So too here. As made clear in the award, the point of which Mr. Lim now makes complaint was much canvassed by both parties to the arbitration. I do not therefore think that it lies in the mouth of Hartela to now argue that the arbitrator exceeded his authority by deciding upon the issue concerning the circular resolution. The proposition contended for has accordingly no application to the circumstances of the present case. It follows that the award is not bad on the ground advanced by Mr. Lim.

Counsel's second complaint is that there is an error of law on the face of the award because the arbitrator held that Hartela was under a duty to warn Ferrostaal of the dangers resulting from the circular resolution. The arbitrator has made it clear in his award that he found for Ferrostaal on the basis of "the best endeavours clause" in the joint venture agreement. Was he right in doing so? I think that he was.

It is settled that parties to a joint venture stand in a fiduciary position to each other. The scope or extent of the duties that joint venturers owe each other depends upon varied considerations. These would encompass (but are not limited to) the nature of the particular joint venture, its subject matter, the relevant documents passing between the parties, including any agreement upon which the particular venture is founded and the attendant circumstances. Here, as in other areas of equity jurisprudence, there is no substitute for a meticulous examination of the facts. If authority is required for these propositions it may be found in the decision of the Supreme Court in *Newacres Sdn Bhd v. Sri Alam Sdn Bhd* [1991] 3 CLJ 2781; [1991] 3 MLJ 474.

It is axiomatic that mutual trust and confidence between joint venturers is essential for the proper working of the relationship. And where, as in the present instance, there is reliance by one joint venturer upon the skill or expertise professed by the other in the subject matter of the enterprise, there is, in my judgment, a duty upon that other to use his best endeavours to ensure the success of the venture. Equity will, in my view, imply such an obligation in the absence of an express term in the particular joint venture agreement.

The joint venture agreement in the present case expressly stipulates such an obligation in the form of the "best endeavours clause". That meant that Hartela was under a duty to use its best endeavours to promote the interests of Hartecon. The circular resolution of 23 March 1983 was not in the best interests of Hartecon. In fact it spelled disaster for Hartecon. Hartela knew that. It was the expert. It should have warned Ferrostaal of the danger. That was the extent of its fiduciary duty. But it failed to warn Ferrostaal. That, in my view, amounts to a breach of the fiduciary duty owed in the circumstances of the present case. The arbitrator so held. He was right.

There is one other matter that requires mention. It has to do with the certificate issued by Mr. Karenmaa. The arbitrator held it to be invalid. He cited several reasons for his finding. I will not go through them all here. Suffice to say that he found the certificate to have come into existence under the most suspicious of circumstances. The certificate was based upon an alleged inspection of the plant and machinery at the factory. Ferrostaal was not invited to join in the examination of the plant and machinery. It knew nothing about the inspection. It therefore had no opportunity to express its views upon the

state of the plant and machinery. Hartela made the call upon the bank guarantee on the basis of the invalid certificate. This led to the eventual collapse of Hartecon.

I am satisfied that on the facts found by the arbitrator Hartela's behaviour in relation to the certificate fell far short of the standard of conduct demanded by a Court of Equity of a fiduciary. That standard was best described by Cardozo CJ, in *Meinhard v. Salmon* [1928] 249 NY 456. 464:

> Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honour the most sensitive is then the standard of behaviour. As to this there has developed a tradition that is unbending and inveterate.

For the reasons expressed thus far I am of opinion that there is no merit in the second and third heads of argument advanced by Mr. Lim. I now turn to address Mr. Lim's fourth and final complaint.

Secret Profit

This part of the case has to do with the Purchase Contract. To recall, Hartela was to supply and install the requisite plant and machinery at Hartecon's factory. But Hartela did not manufacture the machinery. It bought the machinery from a company called Scanmet for RM2,440,000. It then sold the machinery to Hartecon for RM3,364,000. It made a profit of RM924,000 on the transaction. It did not disclose this to Ferrostaal. The arbitrator found that Hartela had breached its fiduciary duty. He ordered Hartela to disgorge the secret profit.

Mr. Lim says that this part of the award is bad in law because the transaction was one of sale of goods. He has argued that a vendor of goods is entitled to make a profit. That, I agree, is true as a general proposition. But here the relationship between Hartela and Ferrostaal was not one of vendor and purchaser simpliciter. They were joint venturers. The purchase contract under which the machinery was sold and delivered was part and parcel of the joint venture. And Hartela as a joint venturer and a fiduciary was not entitled to make a secret profit at the expense of Ferrostaal.

The principle is one of ancient repute in the history of equity jurisprudence. It was established in the well-known case of *Keech v. Sandford* [1726] Sel. Cas. Ch 61. It is that a trustee may not profit from his trust. In the early stages of equity's development the rule was confined to trustees. But it was later extended to all relationships of a fiduciary nature. See, *Aberdeen Ry Co*

v. Blaikie Brothers [1854] 1 Macq. 461. There is no requirement that the fiduciary acted in bad faith in acquiring an advantage for himself. The principle was stated thus by Viscount Sankey in *Regal (Hastings) Ltd. v. Gulliver* [1942] 1 All ER 378, at p. 381:

> In my view, the respondents were in a fiduciary position and their liability to account does not depend upon proof of *mala fides. The general rule of equity is that no one who has duties of a fiduciary nature to perform is allowed to enter into engagements in which he has or can have a personal interest conflicting with the interests of those whom he is bound to protect.* If he holds any property so acquired as trustee, he is bound to account for it to his *cestui que* trust. The earlier cases are concerned with trusts of specific property: *Keech v. Sandford,* per Lord King L.C. The rule, however, applies to agents, as, for example, solicitors and directors, when acting in a fiduciary capacity. (emphasis added.)

It is this doctrine that the arbitrator applied to the fact pattern before him. It follows that the arbitrator's finding was entirely correct.

Miscellaneous Grounds

Counsel for Hartela also raised a number of other subsidiary complaints. These included an attack on the quantum awarded by the arbitrator. It was said that Hartela had been made to account twice. I have examined the award with care. I am unable to find any error of law or misconduct on the part of the arbitrator in respect of these other complaints. It is apparent that the arbitrator when making his award on the quantum took a broad approach. The complaints of Hartela do not in my view fall within the scope of the court's jurisdiction to interfere with arbitration awards.

The Result

It is apparent from the judgment of the learned judge in the court below that he was unimpressed with the arguments raised by Hartela against the validity of the award on liability in the present case. He therefore declined to interfere. So far as the second appeal is concerned, the main ground canvassed before the learned judge was that the arbitrator had become *functus officio* when he handed down the award on liability and was therefore without authority to assess quantum. The learned judge rejected that argument. The point was not pursued at all before this court. Mr. Lim very properly informed us that the object of the second appeal was merely to demonstrate how the arbitrator had misunderstood the whole dispute. There is therefore nothing in the second appeal. It must be dismissed. Having carefully considered the submissions of Mr. Lim who has very ably argued the first appeal I find myself in agreement with the learned judge. The first appeal also fails and I would accordingly

dismiss it. I would also affirm the orders made by the court below in both appeals. The costs of these appeals must be borne by Hartela. The deposits paid into court are to be paid out to Ferrostaal to account of its taxed costs.

My learned brothers Abdul Malek Ahmad and Haidar Mohd. Noor JJCA have seen this judgment in draft and agree with the reasoning and the conclusions therein.